

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE**

In re:

SPORTS AUTHORITY HOLDINGS, INC., *et al.*,<sup>1</sup>

Debtors.

Chapter 11

Case No. 16-10527

Jointly Administered

Re: Docket No. 1092

**DEBTORS' RESPONSE TO TERM LOAN AGENT'S  
EMERGENCY MOTION FOR ADEQUATE PROTECTION**

Sports Authority Holdings, Inc. and its affiliated debtors and debtors in possession (collectively, the "Debtors") in the above-captioned chapter 11 cases (collectively, the "Chapter 11 Cases") hereby submit this response (this "Response") to the *Term Loan Agent's Emergency Motion for Adequate Protection* [Docket No. 1092] (the "Adequate Protection Motion") filed by Wilmington Savings Fund Society, FSB, in its capacity as the Administrative Agent and Collateral Agent for the Term Lenders (the "Term Loan Agent") and respectfully represent as follows:

**PRELIMINARY STATEMENT**

1. The Debtors do *not* object to the Adequate Protection Motion to the extent that the Term Loan Agent seeks an order requiring the Debtors to escrow the Vendor Proceeds so long as the Debtors retain the right to continue to sell the Prepetition Goods. Indeed, the Debtors requested *identical relief* at the outset of the Chapter 11 Cases.

<sup>1</sup> The Debtors and the last four digits of their respective taxpayer identification numbers are as follows: Sports Authority Holdings, Inc. (9008); Slap Shot Holdings, Corp. (8209); The Sports Authority, Inc. (2802); TSA Stores, Inc. (1120); TSA Gift Card, Inc. (1918); TSA Ponce, Inc. (4817); and TSA Caribe, Inc. (5664). The headquarters for the above-captioned Debtors is located at 1050 West Hampden Avenue, Englewood, Colorado 80110.



2. Nonetheless, out of an abundance of caution, the Debtors object to the Adequate Protection Motion to the extent that the Term Loan Agent (a) seeks relief other than in the form of an escrow of the Vendor Proceeds and/or (b) seeks to require the Debtors to provide adequate protection to the extent that the Consigned Goods Motion is denied. With respect to the former, if the Court *grants* the relief requested in the Consigned Goods Motion and/or determines that the Term Loan Agent has an interest in the Prepetition Goods that is senior to the interests therein of the Consignment Vendors, then an escrow of the Vendor Proceeds (which is what the Debtors initially proposed in the Consigned Goods Motion) would adequately protect the Term Loan Agent from any diminution in the value of such proceeds.

3. The converse is equally true. If the Court *denies* the relief requested in the Consigned Goods Motion (thereby finding that the Term Loan Agent's lien in the Prepetition Goods does not prevail over the Consignment Vendors' alleged interests in such Prepetition Goods, or deferring such a finding to a later hearing or proceeding), then the Term Loan Agent will have failed to have met its burden of proof under section 363(p) of the Bankruptcy Code establishing, as a threshold matter, that it has a senior interest in the Prepetition Goods worthy of protection from diminution. In that scenario, the Debtors have no obligation to provide adequate protection to the Term Loan Agent on account of the Prepetition Goods. Given as much, the Debtors do not intend to waste estate resources or the Court's time briefing or arguing the purported "diminution" points raised in the Adequate Protection Motion. Instead, the Debtors reserve all rights in connection therewith and will brief these issues if and when the Court determines, to its satisfaction, that the Term Loan Agent has an interest in Prepetition Goods worthy of protection. It is nonetheless worth noting that the position taken by the Term Loan Agent in the Adequate Protection Motion underplays the substantial adequate protection

(including professional fees, replacement liens, and diminution claims) already being sought for the benefit of the Term Loan Agent pursuant to the DIP Motion (which is set to be heard on the same day as the Adequate Protection Motion).

### **BACKGROUND**

4. On March 2, 2016 (the "Petition Date"), each of the Debtors commenced a voluntary case under chapter 11 of the Bankruptcy Code.

5. On the Petition Date, the Debtors filed the *Motion for Interim and Final Orders (a) Authorizing the Debtors to (i) Continue to Sell Consigned Goods in the Ordinary Course of Business Free and Clear of All Liens, Claims and Encumbrances and (ii) Grant Administrative Expense Priority to Consignment Vendors for Consigned Goods Delivered Postpetition; and (b) Grant Replacement Liens to Consignment Vendors with Perfected Security Interests in Consigned Goods and/or Remit the Consignment Sale Price Arising from Sale of Consigned Goods to Putative Consignment Vendors* [Docket No. 9] (the "Consigned Goods Motion"). Pursuant to the Consigned Goods Motion, the Debtors have sought interim and final orders authorizing the Debtors to, among other things, (a) continue to sell, in the ordinary course of business, free and clear of all liens, claims and encumbrances, certain goods delivered to the Debtors prior to the Petition Date (the "Prepetition Goods") by various vendors (collectively, the "Consignment Vendors") pursuant to certain vendor agreements (collectively, the "Vendor Agreements"), pursuant to section 363(f) of the Bankruptcy Code, and (b) escrow the agreed-upon portion of the proceeds of such Prepetition Goods allocable to the respective Consignment Vendors under the Vendor Agreements (collectively, the "Vendor Proceeds") pending further resolution by the Court.

6. On March 3, 2016 (the “First Day Hearing”), the Court heard argument in support of the Consigned Goods Motion and the objections thereto. In opposing the Consigned Goods Motion, several Consignment Vendors argued, among other things, that they had retained title to the Prepetition Goods that were in the Debtors’ possession. At the conclusion of the First Day Hearing, the Court issued its ruling with respect to the interim relief sought in the Consigned Goods Motion, and upon submission of competing orders from the Debtors and the Consignment Vendors, the Court entered the *Interim Order (A) Authorizing the Debtors to (i) Continue to Sell Consigned Goods in the Ordinary Course of Business Free and Clear of All Liens, Claims, Encumbrances, and Interests; and (ii) Grant Administrative Expense Priority and Purchase Money Security Interests to Consignment Vendors for Consigned Goods Delivered Postpetition; and (B) Grant Replacement Liens to Consignment Vendors with Security Interests and/or Holding Title or Ownership Rights in Consigned Goods and/or Remit the Consignment Sale Price Arising from Sale of Consigned Goods to Putative Consignment Vendors* [Docket No. 278] (the “Interim Order”), denying the Consigned Goods Motion in part, but allowing the Debtors to continue to sell Prepetition Goods under certain circumstances set forth therein.

7. Shortly after the entry of the Interim Order, the Court convened an emergency telephonic conference on March 11, 2016 (the “Emergency Conference”) with the Debtors and certain Consignment Vendors regarding the requirements imposed on the Debtors pursuant to the Interim Order, and entered an order, dated as of March 11, 2016, granting reconsideration of the Interim Order to the extent set forth therein (the “Reconsideration Order”) and scheduling a subsequent hearing on March 16, 2016.

8. On March 16, 2016 (the “Emergency Hearing”), the Court heard argument from the Debtors and certain Consignment Vendors regarding the implementation of the Interim

Order. At the conclusion of the Emergency Hearing, the Court ruled, among other things, that (i) the Debtors are authorized to sell the Prepetition Goods so long as the Debtors comply with the terms of the applicable Vendor Agreements; (ii) the Debtors are directed to remit the Vendor Proceeds to the respective Consignment Vendors pursuant to the terms of the applicable Vendor Agreements in the ordinary course of business; (iii) the Vendor Agreements that were not terminated prior to the Petition Date shall constitute written consent of the applicable Consignment Vendors to the sale of the applicable Prepetition Goods by the Debtors; (iv) all parties in interest shall reserve all other rights under the Bankruptcy Code or applicable law; and (v) to the extent that any of the Debtors are party to a Vendor Agreement that was terminated prior to the Petition Date, the Debtors shall comply with applicable law. The Debtors reserved the right to seek disgorgement of Vendor Proceeds remitted to the applicable Consignment Vendors to the extent that the Court (or an appellate court) ruled that any such Consignment Vendor does not hold an interest in the applicable Prepetition Goods that is senior to the rights of the Debtors' estates or the Secured Lenders (as defined below). The Court requested that the Debtors draft and submit a proposed form of order (the "Supplemental Interim Order") memorializing the Court's ruling, and overruled all objections to, and solely to the extent necessary for, the entry of the Supplemental Interim Order.

9. Following the conclusion of the Emergency Hearing, the Debtors negotiated the form of the Supplemental Interim Order with the Consignment Vendors, on the one hand, and each of the ABL DIP Lenders, the FILO DIP Lenders, and the Term Lenders (collectively, the "Secured Lenders"), on the other hand. On March 31, 2016, the Debtors, the Consignment Vendors, and the Secured Lenders convened a joint conference call to finalize the form of Supplemental Interim Order, which the Debtors subsequently filed with the Court under

certification of counsel on April 1, 2016 [Docket No. 943]. The Court approved and signed the Supplemental Interim Order on April 5, 2016 [Docket No. 1044].

10. On March 15, 2016 and March 16, 2016, certain of the Debtors filed a total of 160 complaints (collectively, the “Complaints”), commencing adversary proceedings against certain Consignment Vendors. Pursuant to the Complaints, the Debtors seek, among other things, a declaratory judgment with respect to (i) the Debtors’ superior rights and interests in the Prepetition Goods vis-a-vis the applicable Consignment Vendors, and (ii) the Debtors’ ability to sell the Prepetition Goods, in each case pursuant to applicable provisions of the Bankruptcy Code and applicable provisions of the Uniform Commercial Code (collectively, the “Adversary Proceedings”).

**A. The Debtors’ Settlement Motion**

11. As a result of negotiations with the Debtors, certain material Consignment Vendors, measured by the amount of Prepetition Goods delivered by each such Consignment Vendor (collectively, the “Consenting Vendors”) each delivered an executed settlement agreement (collectively, the “Settlement Agreements”) intended to, among other things, (a) resolve the applicable Adversary Proceedings against such Consenting Vendors and (b) facilitate deliveries of goods by such Consenting Vendors after the Petition Date (the “Postpetition Goods”). On April 1, 2016, the Debtors filed the *Motion for an Order, Pursuant to Section 105(a) of the Bankruptcy Code and Bankruptcy Rule 9019, Approving the Settlement Agreement Between the Debtors and Certain Consignment Vendors Party Thereto* [Docket No. 959] (the “Settlement Motion”), seeking, among other things, entry of an order (a) approving and authorizing the Debtors to enter into and consummate the Settlement Agreements with the Consenting Vendors and any Subsequent Consenting Vendors (as defined in the Settlement Motion) and (b) granting automatic, perfected, senior security interests in any Postpetition Goods

and the respective Vendor Proceeds to the applicable Consignment Vendors that deliver any Postpetition Goods. As of the date hereof, approximately 27 Consignment Vendors delivered executed Settlement Agreements to the Debtors.

**B. The Adequate Protection Motion**

12. On April 8, 2016, the Term Loan Agent filed the Adequate Protection Motion. Pursuant to the Adequate Protection Motion, the Term Loan Agent demands adequate protection to compensate the Term Loan Agent for the alleged diminution of the value of its alleged collateral allegedly caused by the remittance of the Vendor Proceeds to the applicable Consignment Vendors on account of sold Prepetition Goods on and after the Petition Date, in compliance with the Supplemental Interim Order. In the Adequate Protection Motion, the Term Loan Agent asserts: “Based on the available evidence . . . the only practicable way for the Debtors to provide adequate protection is for the Debtors to continue to sell the [Prepetition Goods] and place the proceeds of such sales in escrow pending a final determination by the Court as to which parties have senior rights in such proceeds.” This request for adequate protection—establishing an escrow account for the Vendor Proceeds—mirrors the relief that the Debtors have requested in the Consigned Goods Motion, which the Court has denied on an interim basis in the Interim Order and the Supplemental Interim Order.

13. Pursuant to the Adequate Protection Motion, the Term Loan Agent also revisits its opposition to the Supplemental Interim Order (as memorialized in its appeal of the Supplemental Interim Order to the United States District Court (the “District Court”) and its motion for a stay of the Supplemental Interim Order pending appeal, which was denied both by this Court and the District Court) and the ability of the Debtors to remit the Vendor Proceeds in compliance therewith. Finally, the Adequate Protection Motion foreshadows the Term Loan Agent’s objection to the Settlement Motion (discussed below).

14. Importantly, the Adequate Protection Motion is predicated on the presumption that the Debtors and the Secured Lenders will prevail in the Adversary Proceedings and will be deemed to have superior rights in the Prepetition Goods relative to the rights asserted therein by the applicable Consignment Vendors.

**C. The Term Loan Agent’s Objection to the Debtors’ Settlement Motion**

15. On April 12, 2016, the Term Loan Agent filed its *Objection to Debtors’ Motion for an Order, Pursuant to Section 105(a) of the Bankruptcy Code and Bankruptcy Rule 9019, Authorizing the Settlement Agreement Between the Debtors and Certain Consignment Vendors Party Thereto* [Docket No. 1139] (the “Settlement Objection”). The Settlement Objection restates the Term Loan Agent’s arguments in the Adequate Protection Motion and its opposition to the Supplemental Interim Order, and attacks the Settlement Motion based on arguments that have already been advanced by the Debtors in support of the Consigned Goods Motion and/or are pending before the Court in the context of the Adversary Proceedings. Like the Adequate Protection Motion, the Settlement Objection necessarily *presumes* an outcome in the Adversary Proceedings that is favorable to the Debtors and the Secured Lenders vis-a-vis the Consignment Vendors.

**D. Recent Developments and the Debtors’ Withdrawal of the Settlement Motion**

16. Due to recent developments in the Chapter 11 Cases and the sale process that the Court approved on April 14, 2016 [Docket No. 1186], the Debtors determined that the best path forward to maximize value for all stakeholders in the upcoming auction and sale was to withdraw its support of the Settlement Motion. *See Notice of Withdrawal of Docket No. 959* [Docket No. 1257] (the “Withdrawal Notice”).



**LIMITED OBJECTION**

**A. The Debtors Do Not Object to an Escrow Account for the Vendor Proceeds**

17. The Debtors requested, at the outset of the Chapter 11 Cases, the authority to sell the Prepetition Goods and place the Vendor Proceeds in an escrow account pending further resolution by the Court while preserving all rights of parties in interest. Given the Withdrawal Notice, the Debtors have no objection to the establishment of an escrow account for the Vendor Proceeds (an “Escrow Account”) pending resolution by the Court of the Adversary Proceedings. The Debtors agree with the Term Loan Agent that an Escrow Account is a reasonable and practical approach to the treatment of the Prepetition Goods pending the resolution of the disputed and competing rights and interests in the Prepetition Goods raised in the Adversary Proceedings.

18. Accordingly, so long as the Debtors retain the right to sell the Prepetition Goods, the Debtors have no objection to placing the Vendor Proceeds into an Escrow Account and preserving all parties’ rights therein pending resolution of the Adversary Proceedings.

**B. The Term Loan Agent’s Request for Additional Adequate Protection Is Unwarranted and Premature**

19. To the extent that, pursuant to the Adequate Protection Motion, the Term Loan Agent seeks adequate protection in addition to the relief requested in the Consigned Goods Motion, the Debtors object to the Adequate Protection Motion on the grounds that such additional adequate protection is unwarranted, or at best, premature unless and until the Adversary Proceedings are favorably resolved vis-a-vis the Term Loan Agent. Therefore, such additional adequate protection must be denied at this time as a matter of law.

20. Section 363(e) of the Bankruptcy Code provides that “[n]otwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used,

sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest.” 11 U.S.C. § 363(e).

21. Section 363(p)(2) provides that “the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest.” 11 U.S.C. § 363(p)(2). This is not surprising because, before a debtor is obligated to provide adequate protection for the diminution of value of interest, there must be a proven interest that needs protection. *See, e.g., In re Vista Mktg. Grp., Ltd.*, 2016 WL 1254999, at \*15 (Bankr. N.D. Ill. Mar. 30, 2016) (“While the trustee or debtor-in-possession ‘has the burden of proof on the issue of adequate protection,’ the ‘entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest.’”) (citing 11 U.S.C. § 363(p)); *In re Oak Rock Fin., LLC*, 527 B.R. 105, 114 (Bankr. E.D.N.Y. 2015) (“Pursuant to 11 U.S.C. § 363(p)(2), [the creditor] has the burden of proof regarding the validity, priority or extent of its lien.”); *In re Isaacson Steel, Inc.*, 2013 WL 5310550, at \*5 (Bankr. D.N.H. Sept. 19, 2013) (“‘An entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest.’ Parties claiming an interest in proceeds of a sale of a debtor’s assets have the burden of showing an interest by a preponderance of the evidence.”) (citations omitted); *In re Premier Golf Missouri, LLC*, 2012 WL 2803732, at \*2 (Bankr. W.D. Mo. July 6, 2012) (“Section § 363(p) dictates which party has the burden of proof and provides that ‘the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest.’”); *In re Las Vegas Monorail Co.*, 429 B.R. 317, 328 (Bankr. D. Nev. 2010) (“The Ninth Circuit has held that a party seeking to establish the “extent” of its interest in property under § 363(p)(2) must satisfy a two-prong test: First, as a preliminary

matter, the party must prove that it holds a perfected security interest in post-petition revenues to which its liens still rightly attach. Second, a party must prove the amount of money to which its liens attach.”).

22. In *In re R.J. Dooley Realty, Inc.*, the court explained that “[t]he purpose of adequate protection is to guard a secured creditor against any decrease in the value of its collateral resulting from depreciation, destruction or the debtor’s use of the collateral.” 2010 WL 2076959, at \*8 (Bankr. S.D.N.Y. May 21, 2010). For this reason, “Bankruptcy Code § 363(p)(2) provides that the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of *its* interest.” *Id.* (emphasis added). For instance, in *In re Premier Golf*, the chapter 11 trustee sought authority to sell certain assets that were located on the debtor’s golf club to the winning bidder of the court-approved bidding and sale process. 2012 WL 2803732, at \*2. The manager of the debtor’s golf club (and managing member of the debtor) objected to the proposed sale and sought adequate protection, alleging an ownership interest in the assets to be sold. *Id.* The court held that “the [manager] bears the burden of proving its ownership interest in the Disputed Assets.” *Id.* After analyzing applicable state law and applying it to the evidence presented, the court concluded that the assets at issue were owned by the debtor and could be sold to the winning bidder, and that the manager had not met its burden of proof under section 363(p)(2). *Id.* at \*6.

23. Here, before the Adversary Proceedings are resolved, the Term Loan Agent cannot demonstrate the priority of its asserted interest in the Prepetition Goods. Indeed, the validity, priority and extent of the interests in the Prepetition Goods asserted by the Consignment Vendors vis-a-vis the Debtors and/or the Secured Lenders is squarely before the Court in the Adversary Proceedings and have yet to be decided. Therefore, the Term Loan Agent is unable to

satisfy its burden of proof with respect to its prior interest in the Prepetition Goods. Put another way, the Term Lenders have shown no “interest in property” under section 363(p)(2) that the Debtors must adequately protect from diminution under section 363(e).

24. Nonetheless, as noted above, the Debtors do not object to the use of an Escrow Account for the Vendor Proceeds, and do not object to the preservation of all parties’ rights in the Prepetition Goods, including the Term Loan Agent’s rights to assert and prove its right to adequate protection pending resolution of the Adversary Proceedings. However, requiring the Debtors to provide additional adequate protection at a time when the Term Loan Agent is unable to satisfy the threshold requirement in section 363(p)(2), is premature at best, and puts the cart before the horse.

*[Remainder of Page Intentionally Left Blank]*

WHEREFORE, the Debtors respectfully request that the Court deny the relief in the Motion to the extent that it seeks additional adequate protection for the Term Loan Agent other than as set forth in the Consigned Goods Motion.

Dated: April 22, 2016  
Wilmington, Delaware

/s/ Andrew L. Magaziner

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